



INDIAN REAL ESTATE INDUSTRY OUTLOOK

30 July 2019

INDUSTRY OUTLOOK

The real estate sector is broadly classified into three segments viz. Residential, Commercial and Retail-Malls. There are 8 major real estate markets in the country, with Mumbai, NCR and Bengaluru being the top cities, followed by Pune, Hyderabad, Chennai, Kolkata and Ahmedabad. India's rank in the Knight Frank's Global House Price Index has jumped 13 spots above to reach the 9th position among 55 international markets in the second-quarter of 2017 over June 2016 on the back of increasing prices in mainstream residential sector¹.

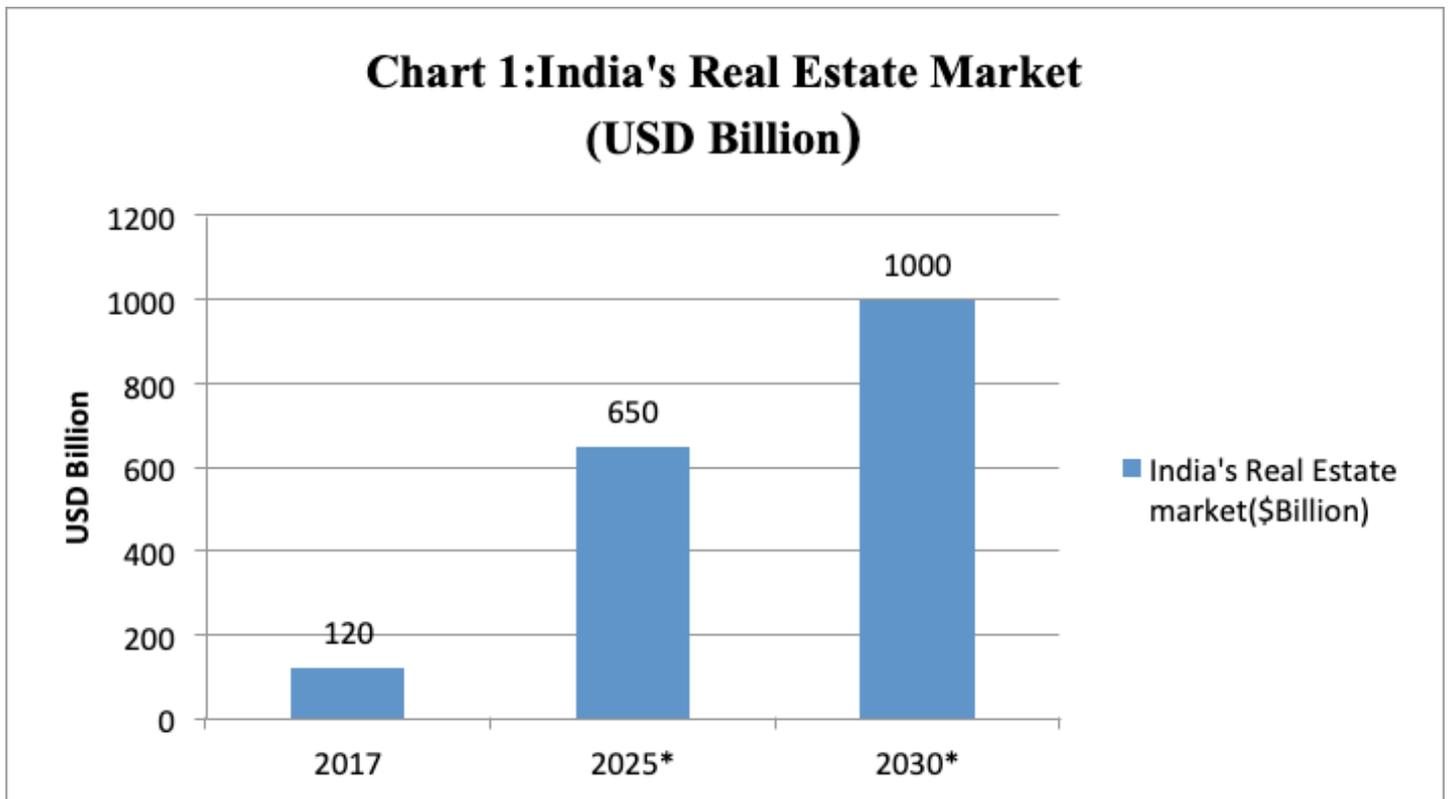
Table 1: Various Segments of Real Estate Market

| Sl No. | Segments | Details/Description |
|--------|-------------------|---|
| 1 | Residential Space | Residential segment contributes ~80 per cent of the real estate sector. Housing launches across top eight Indian cities increased 75 per cent in 2018 to 182,207 units. |
| 2 | Commercial Space | Few Players with presence across India; Most of the activity is in the leasing segment. |
| 3 | Retail Space | FDI in multibrand retail to boost demand; The retail segment in Indian realty attracted Private Equity (PE) investments of around INR 5,500 crore between 2015 to March 2018. Around 5.1 million sq.ft.of retail space became operational into seven Indian cities in 2018. |
| 4 | Hospitality Space | Hotel room supply in the country increased 7.5percent in FY18. |
| 5 | SEZs | As of January 22,2019, India had formally approved 421 SEZs |

MARKET SIZE

Real estate sector in India is expected to reach a market size of US\$ 1 trillion by 2030 from US\$ 120 billion in 2017 and contribute 13 per cent of the country's GDP by 2025. Retail, hospitality and commercial real estate are also growing significantly, providing the much-needed infrastructure for India's growing needs.

Sectors such as IT and ITeS, retail, consulting and e-commerce have registered high demand for office space in recent times. Commercial office stock in India is expected to cross 600 million square feet by 2018 end while office space leasing in the top eight cities is expected to cross 100 million square feet during 2018-20. Co-working space across top seven cities has increased sharply in 2018 (up to September), reaching 3.44 million square feet, compared to 1.11 million square feet for the same period in 2017.

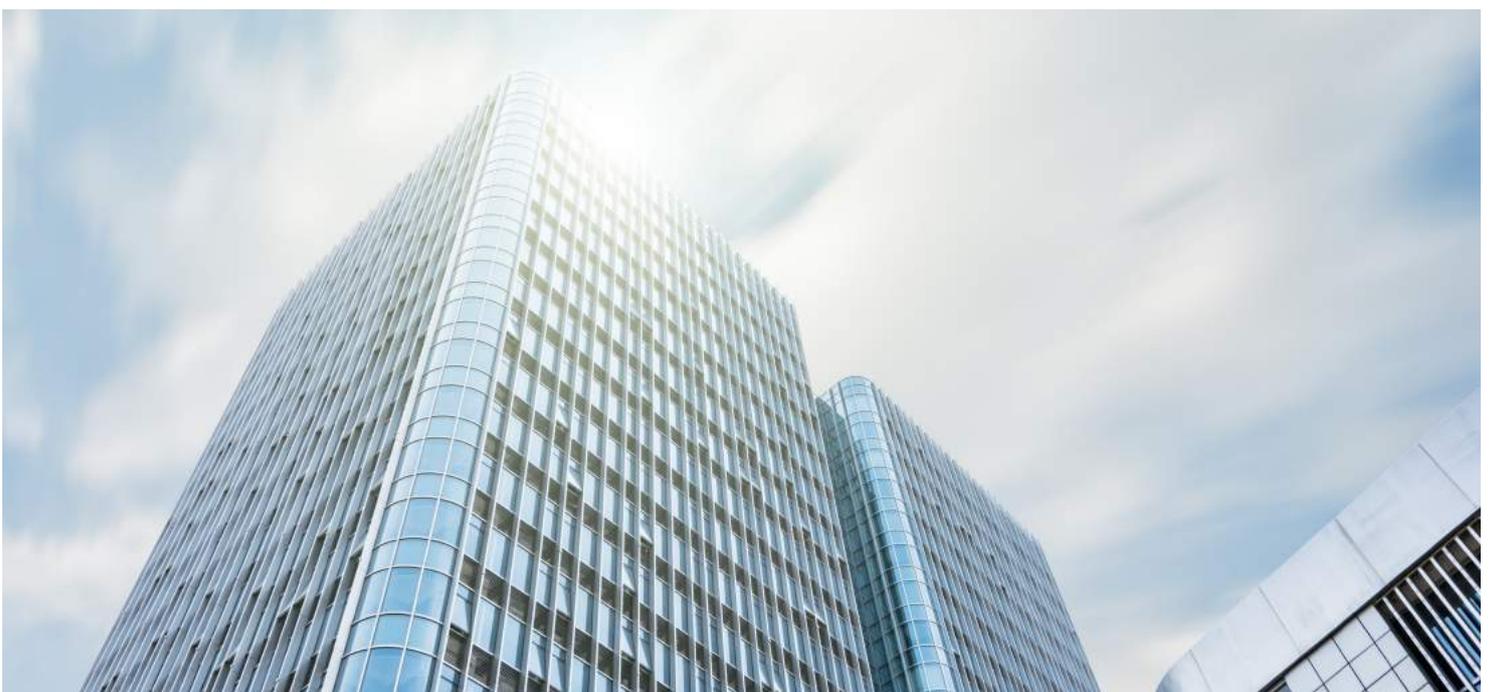


*Note: values for 2025 and 2030 are estimated values.

Source: 'Real Estate' (March 2019) India Brand Equity Foundation (IBEF) <https://www.ibef.org/download/real-estate-mar-2019.pdf>

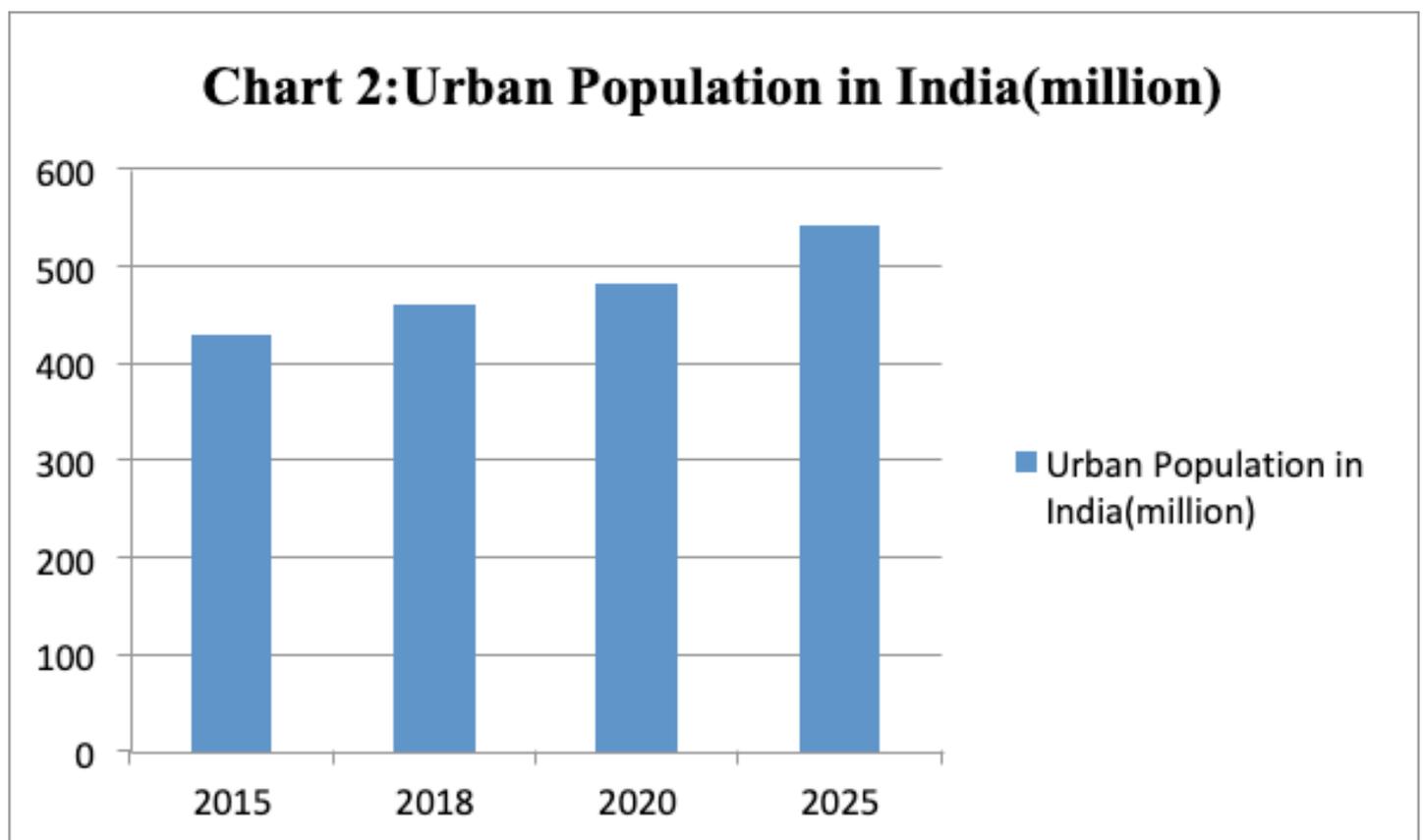
GOVERNMENT INITIATIVES

- Under the Pradhan Mantri Awas Yojana (PMAY) Urban, more than 6.85 million houses have been sanctioned up to December 2018.
- In February 2018, creation of National Urban Housing Fund was approved with an outlay of Rs 60,000 crore (US\$ 9.27 billion).
- In the Union Budget 2019-20, the Government of India has extended benefits under Section 80-IBA of the Income Tax Act till March 31, 2020 to promote affordable housing in India².
- Real Estate Investment Trusts (REITs) in non-residential segment and Infrastructure Investment Trusts. REIT will open channels for both commercial and infrastructure sector. In March 2019, Embassy Office Parks India's first REIT, went public³.
- The Union Budget 2019-20 provided the following incentives for the real estate sector⁴.
 - Deduction of interest for affordable housing: In order to incentivize purchase of affordable house, it is proposed to provide a deduction upto Rs. 1,50,000 for interest paid on loan taken for purchase of residential house having value upto Rs. 45 lakh. This shall be in addition to the existing interest deduction of Rs. 2 lakh.
 - Alignment of definition of affordable housing with GST Acts: In order to align the definition of affordable housing in the Income-tax Act with the GST Acts, it is proposed to increase the limit of carpet area from 30 square meters to 60 square meters in Metropolitan regions and from 60 square meters to 90 square meters in non-metropolitan regions. It is also proposed to provide the limit on cost of the house at Rs. 45 lakh in line with the definition in the GST Acts.



GROWTH DRIVERS

- Demand for residential properties has surged due to increased urbanisation and rising household income. Indian government's smart city projects (100 smart cities to be built by 2020)⁵.
- India is among the top 10 price appreciating housing markets internationally. Growing requirements of space from sectors such as education and healthcare, e-commerce and logistics also giving thrust to the industry.
- Warehousing space in top eight Indian cities increased 22 per cent y-o-y in 2018 to 169 mn sq. ft. Investments of Rs 50,000 crore (US\$ 7.76 billion) are expected in India's warehousing between 2018-20.
- The government has allowed FDI of up to 100 per cent for townships and settlements development projects. Under the Housing For All Scheme, 60 million houses are to be built which include 40 million in rural areas and 20 million in urban area by 2022. Significant increase in real estate activity in cities like Indore, Raipur, Ahmedabad, Jaipur and other 2-tier cities; this has opened new avenues of growth for the sector.

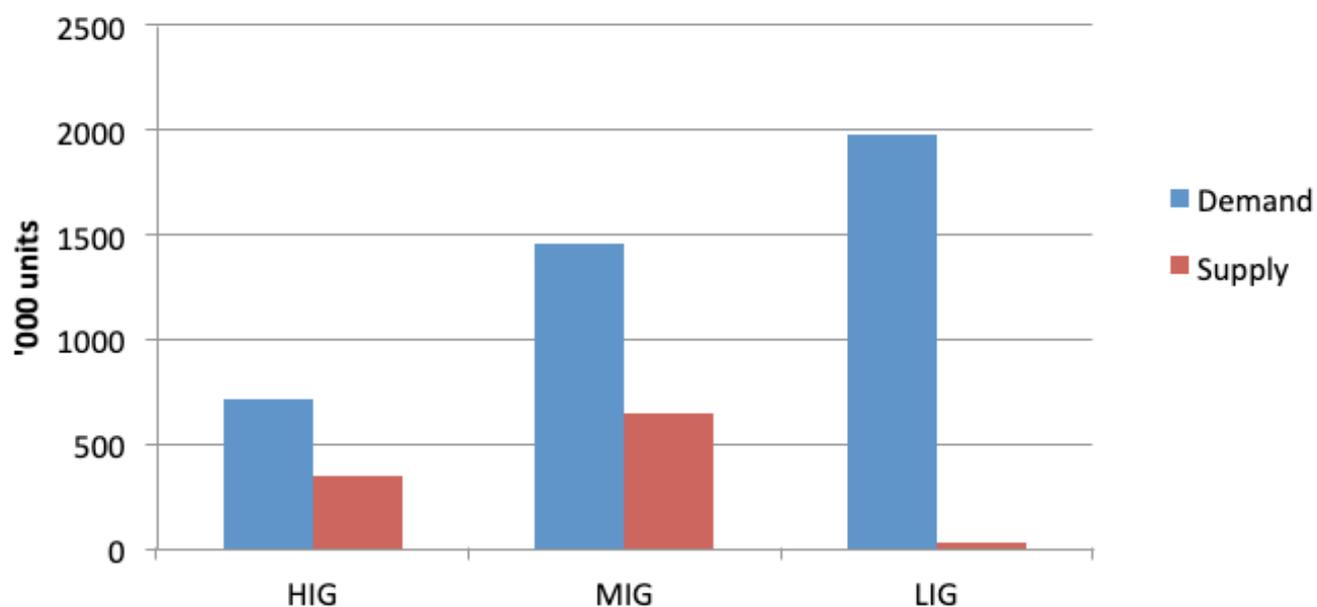


Source: Compiled from IBEF (March 2019)

Table 2: Demand for Residential Space Expected to increase

| | |
|-----------------------|---|
| Scenario | <p>A localised, fragmented market presents opportunities for consolidation with only few large, pan-India players such as DLF.</p> <p>More foreign players might enter the market as FDI norms have eased.</p> |
| Key Drivers | <p>Rapid Urbanization</p> <p>Population Growth</p> <p>Increase in nuclear families</p> <p>Easy availability of finance</p> <p>Repatriation of NRIs and HNIs</p> <p>Rise in disposable income</p> |
| Notable Trends | <p>National Capital Region (NCR) is expected to generate maximum demand in MIG and HIG category followed by Bengaluru.</p> <p>Developers are focusing on affordable and mid-range categories to meet increasing demand.</p> |

Chart 3: Cumulative Housing Demand-Supply in Top Eight Cities(2016-20)in '000 units



Source: Compiled from IBEF (March 2019)

Table 3: Metros driving demand for commercial space

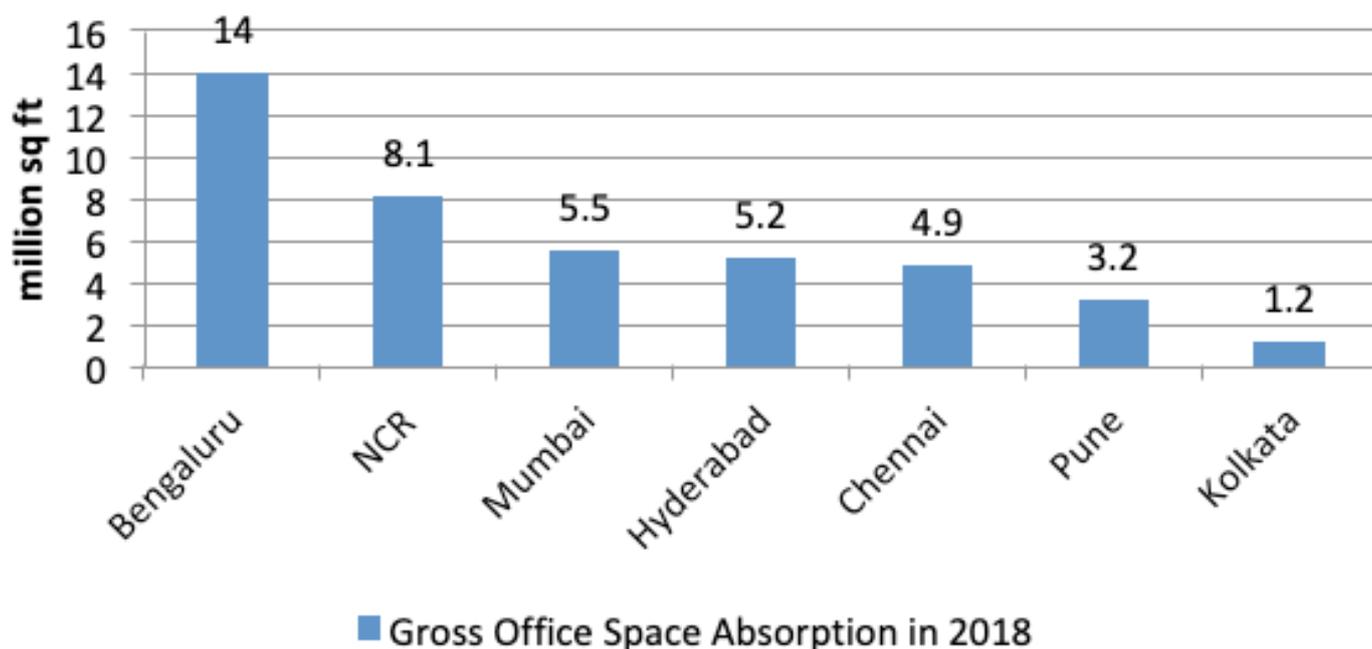
| | |
|-----------------------|--|
| Scenario | Few large developers with a pan-India presence dominate the market. Operating model has shifted from sales to a lease and maintenance |
| Key Drivers | Rapid growth in services sectors: IT/ITeS, BFSI and Telecom. Rising demand from MNCs. Demand for office space in Tier-II cities. |
| Notable Trends | Co-working space across top seven cities has increased sharply in 2018 (up to September), reaching 3.44 million square feet, compared to 1.11 million square feet for the same period in 2017. |

OFFICE MARKET OVERVIEW

Office market has been driven mostly by growth in ITeS/IT, BFSI, consulting and manufacturing. Moreover, many new companies are planning a foray into Indian markets due to huge potential and recently relaxed FDI norms. Grade A office space absorption is expected to cross 600 million square feet by 2022, with Delhi-NCR contributing to most of its demand. Gross office absorption in top Indian cities has increased 26 per cent year-on-year to 36.4 million square feet during January – September 2018.



**Chart 4: Gross Office Space Absorption in 2018
(million Square feet)**



Source: 'Real Estate' (March 2019) India Brand Equity Foundation (IBEF) <https://www.ibef.org/download/real-estate-mar-2019.pdf>

| Items | 2018 (million sq ft) | Per Cent Growth (year on year) | 2019 (million sq ft) | Per Cent Growth (year on year) |
|----------------|-------------------------|--------------------------------------|-------------------------|--------------------------------------|
| Net Absorption | 33.3 | 16% | 37.4 | 12% |
| New Completion | 38 | 41% | 43.6 | 15% |
| Vacancy | 14% | — | 14% | — |

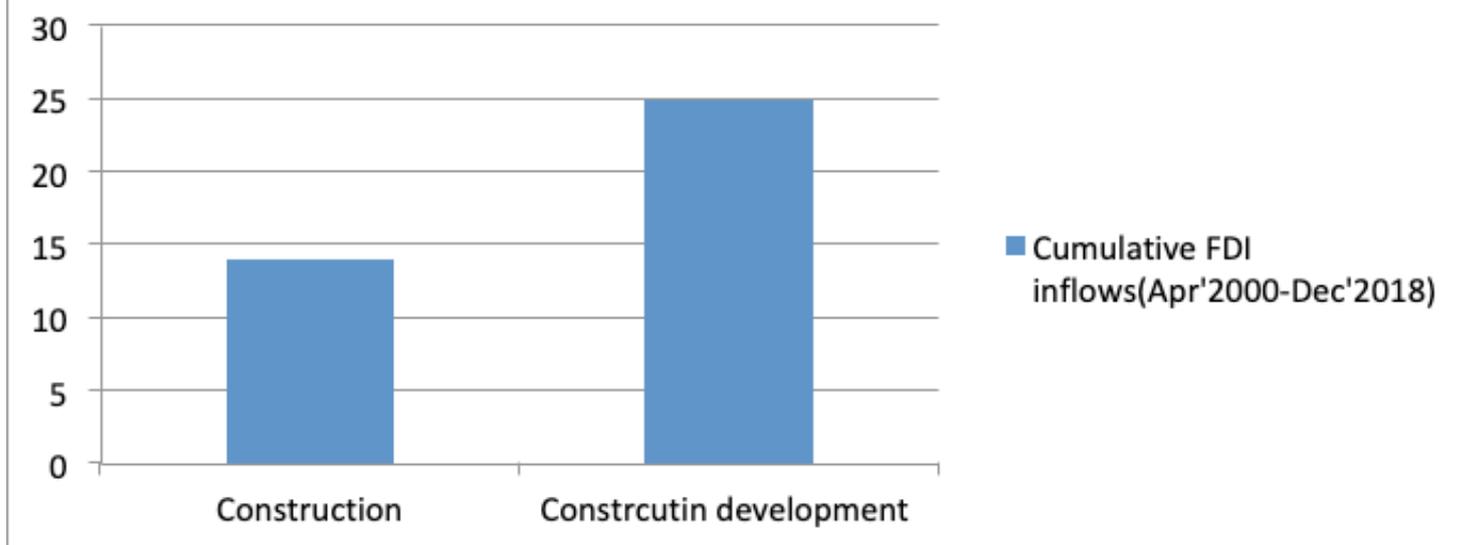
Source: JLL, REIS Estimate

The office market exhibited healthy growth of 16% in 2018 with net absorption estimated to cross 33 mn sq ft during the year. This trend is likely to continue, with net absorption expected to surpass 37 mn sq ft by the end of 2019. As focus gradually shifts to the development of modern offices that meet the aspirations of new age occupiers, the market will see more such supply in the coming quarters. Hence, there will be a change in the proportion of Grade A stock in the decentralized markets. This would result in the emergence of alternate Central Business Districts (CBDs) in and around cities. Bengaluru dominated the net take up in office spaces followed by Mumbai and Delhi/NCR. These three markets accounted for 66% of the demand in office spaces across the top seven cities in the country. A significant change in occupier trends has been witnessed with a marked increase in the collective take up of co-working spaces. The share of co-working spaces in total office leasing increased to 10% in 2018 from 5% in 2017. With more supply likely to come in the near future, leasing activity is expected to intensify in 2019. In addition to the strong demand from start-ups and SMEs, large mainstream corporates are also actively looking at these new age office spaces.

RETAIL SPACE LIKELY TO SEE GROWTH

At present, Retail accounts for a small portion of the real estate market. However, the growing consumerism, growth of organized retail sector in India, entry of MNC retailers is important growth drivers. Around 32 new malls with area of 13.5 million square feet are expected to start operations in 2019. Mumbai, National Capital Region (NCR), Bengaluru, Kolkata witnessed highest growth in retail real estate during 2018.

Chart 5: Cumulative FDI inflows in Construction & Construction Development Industry (Apr'2000-Dec'2018)



Source: 'Real Estate' (March 2019) India Brand Equity Foundation (IBEF) <https://www.ibef.org/download/real-estate-mar-2019.pdf>

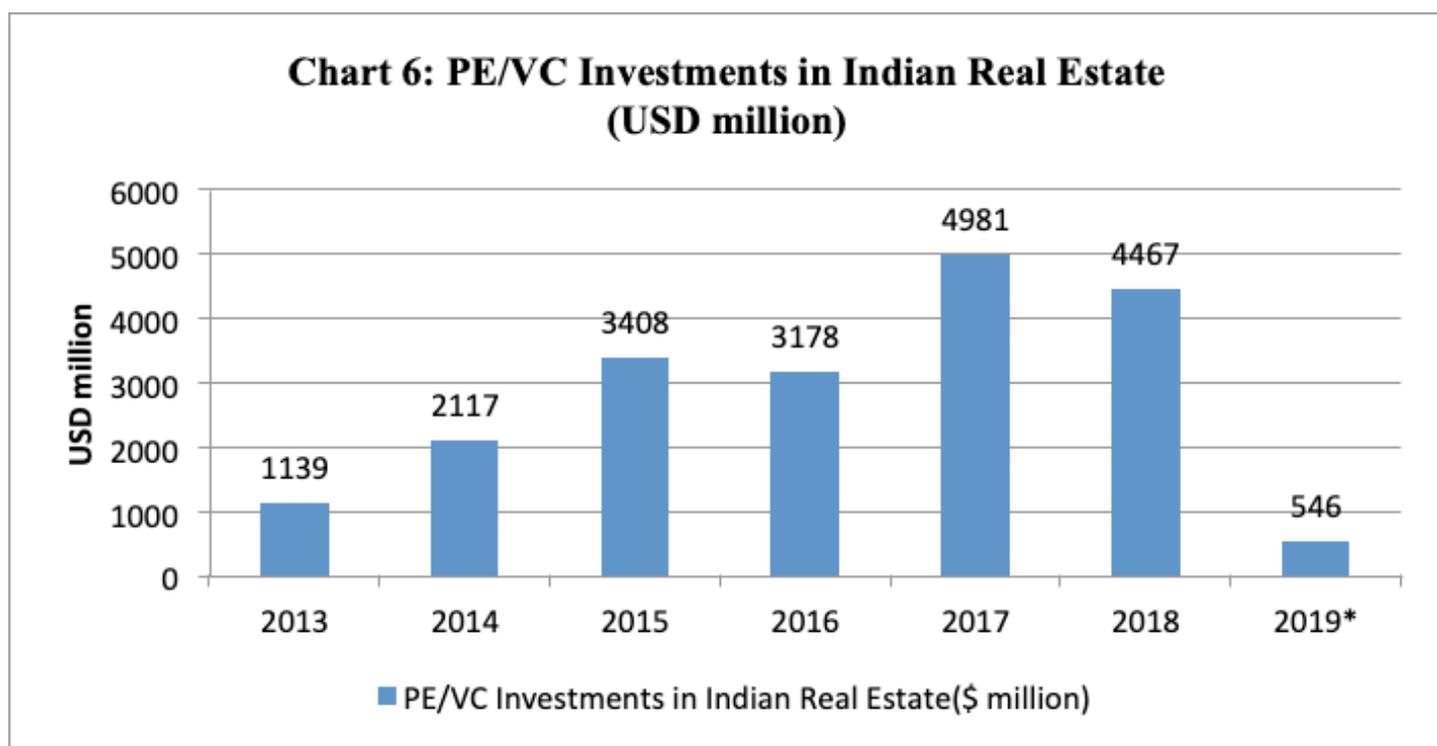
INVESTMENTS/DEVELOPMENTS

The Indian real estate sector has witnessed high growth in recent times with the rise in demand for office as well as residential spaces. Between 2009-18*, Indian real estate sector attracted institutional investments worth US\$ 30 billion. Private Equity and Venture Capital investments in the sector reached US\$ 4.47 billion in 2018 and US\$ 546 million in Jan-Feb 2019.

According to data released by Department of Industrial Policy and Promotion (DIPP), the construction development sector in India has received Foreign Direct Investment (FDI) equity inflows to the tune of US\$ 24.91 billion in the period April 2000-December 2018.

Some of the major investments and developments in this sector are as follows:

- Housing launches across top eight Indian cities increased 75 per cent in 2018 to 182,207 units.
- In March 2019, Embassy Office Parks, India's first real estate investment trust (REIT) went public.
- Warehousing space in top eight Indian cities increased 22 per cent y-o-y in 2018 to 169 mn sq. ft.
- Around 5.1 million sq. ft. of retail space became operational in top seven Indian cities in 2018.
- In May 2018, Blackstone Group acquired One Indiabulls in Chennai from Indiabulls Real Estate for around Rs 900 crore (US\$ 136.9 million).
- In February 2018, DLF bought 11.76 acres of land for Rs 15 billion (US\$ 231.7 million) for its expansion in Gurugram, Haryana.

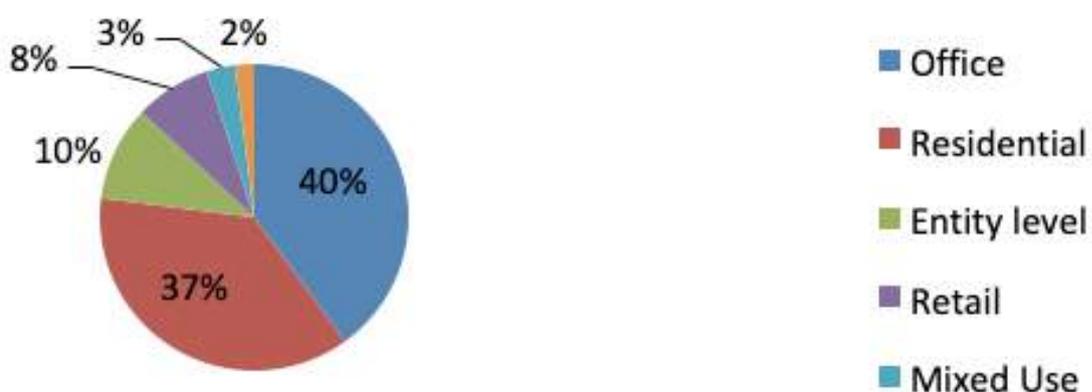


*Up to February 2019.

PE: Private Equity; VC: Venture Capital Source: India Brand Equity Foundation report on Real Estate(March 2019).

Between 2009-18⁶, Indian real estate sector attracted institutional investments worth US\$ 30 billion. Private Equity and Venture Capital investments in the sector reached US\$ 4.47 billion in 2018. In 2018, Indospace raised US\$ 1.2 billion to build logistics parks, the largest investment during the year.

Chart 7: Distribution of Institutional Investments in India(2014-18)



Source: India Brand Equity Foundation report on Real Estate(March 2019).

Table 4: Top Deals in H1 2019 (USD million)

| Investor | Investee | Deal Value | City | Sector |
|------------------|--------------|------------|-----------------|--------|
| Warbug Pincus | Runwal Group | 1,000 | Multiple Cities | Retail |
| Kotak Investment | Divyasree | 400 | Multiple Cities | Office |
| Blackstone | Radius | 330 | Mumbai | Office |

Source: Colliers International

Foreign funds remain active in the real estate market, with inflows from such investors rising 28 per cent in H1 2019. While foreign funds continue to be active in the commercial office space, they are also investing into the logistics sector. Some recent funds in this space include Logos, Morgan Stanley and the Warburg Pincus-backed developer e-Shang Redwood. Mumbai, India's financial capital, accounted for 27% of total inflows, garnering roughly USD 1.05 billion (INR7,288 crore) of investments. Most of those investments made in the city were on the project level, allowing investors lower risk and appetite. Pune also attracted notable investments during the six-month period, led by office sector, followed by residential assets and retail malls.

Real Estate Investors are opting for Tier 2 and Tier 3 cities

As per a consumer survey 26 per cent of property investors prefer Tier 2 and Tier 3 cities with Ahmedabad, Jaipur, Chandigarh, Nashik and Kochi ranking among the new preferred destinations, one of the major reasons for such investments is lack of affordability of major cities. The 'smart city' tag is also believed to be driving this change – these cities are supported by government initiatives like smart cities and AMRUT the implementation of which has been smoother than in Tier 1 cities.

Real Estate Trends Expected to Emerge in 2019

2019 is expected to be another tough year for real estate developers, given the ongoing liquidity problem, owing to the NBFC crisis. However, even as the scenario remains bleak, some new trends are expected to emerge during the year, as follows⁷:

Affordable housing

In the last couple of years, affordable housing is the only segment where transactions seem to be happening. The trend is expected to continue in 2019. Government incentives to both developers and homebuyers are pushing supply as well as demand within the segment. The government extended the benefit of Credit Link Subsidy Scheme (CLSS) on home loans for the Middle Income Group (MIG) under the Pradhan Mantri Awas Yojana (Urban) till the end of March 2020. A homebuyer can avail a subsidy of up to ₹ 2.67 lakh on home loans under this scheme.

Co-living options

Co-living is not a new concept, but just got a new name recently. Many people, especially students and young professionals, prefer to share a house or apartment, usually with other students or professionals. Various privately-operated hostels or lodges work on the basic concept of co-living.



While such co-living trends have been around for several years now, they are getting more organised now. While it is largely major cities like Bengaluru, Mumbai, Gurgaon and Pune that began promoting this concept, the demand for co-living spaces is also gradually percolating to tier II cities like Jaipur and Lucknow where both working millennials and students are increasingly opting for these spaces. Co-living is a fragmented industry with most players being startups having formed in the last 3-4 years. Nestaway, Oyo Living, ZiffyHomes, StayAbobe, SimplyGuest, Placio, YourOwnROOM, RentMyStay, CoHo, CoLive, Stanza Living, Quickr, and Zolo are the key players operating in this space.

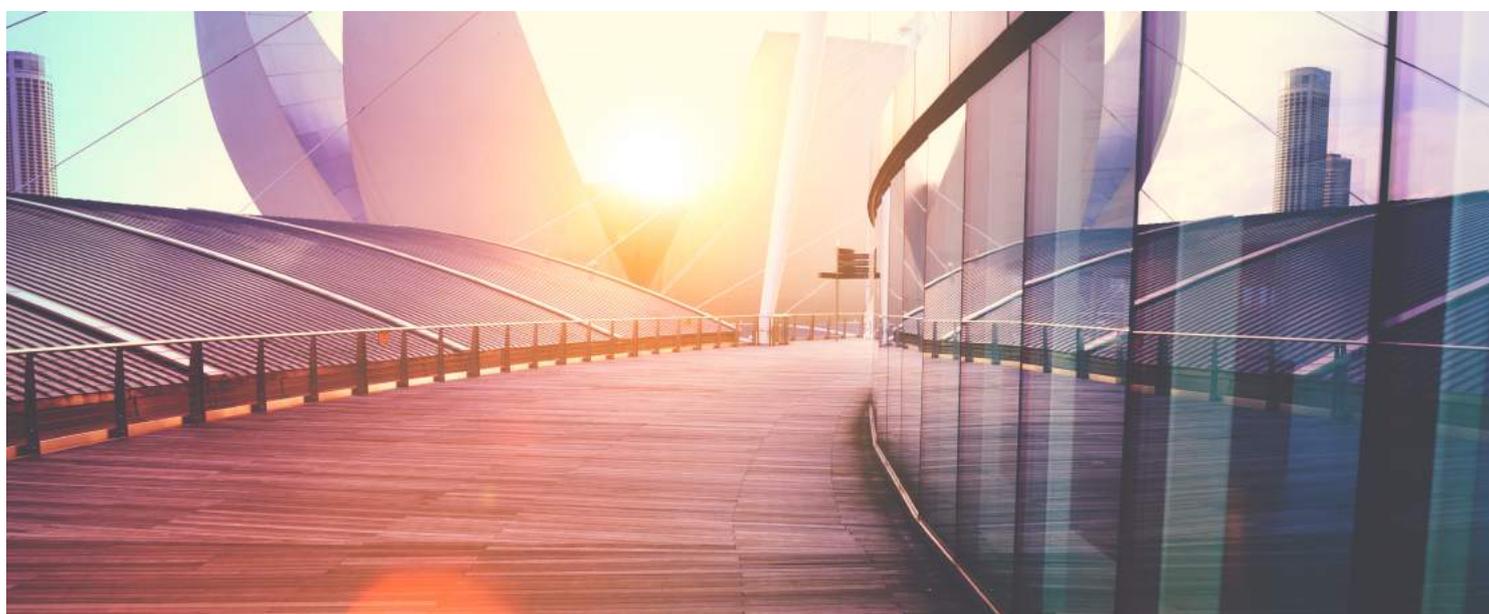
Co-working spaces

As far as commercial real estate is concerned, co-working spaces are expected to strengthen their position in 2019. It was a new concept in India a decade ago, but not anymore. In the last few years, co-working spaces have witnessed a lot of traction and acceptability. While earlier only small businesses and individual professionals opted for it, now even larger companies are occupying co-working spaces. The share of co-working spaces in total office leasing increased to 10% in 2018 from 5% in 2017. With more supply likely to come in the near future, leasing is expected to intensify in 2019. In addition to strong demand from startups and small and medium enterprises (SMEs), large mainstream corporates are also actively looking at these new-age office spaces.



INDUSTRY RISK

Indian developers face stress as the credit market dries up; borrowing rates for most developers have increased substantially in more than a decade. After the shocking default by the IL&FS Group, many mortgage lenders are struggling to roll over debt amid downgrades in their credit ratings. Shadow banks that lent heavily to developers in recent years are among the worst hit, as the recovery in housing sales remains tepid. The cash crunch has raised questions around solvency of real-estate companies and threatens to push 70 per cent of such companies out of business in next two years. Challenges to paying debt obligations amid a slump in apartment sales might force developers to sell assets. Whereas, there are pre-sanctioned limits on various projects, but disbursement is not happening as per the committed amount. Decision-making at lenders is also taking long time. Issues regarding actual implementation of Real Estate and Regulation Act (RERA) by various states also pose challenges. The central law RERA provided the basic framework of consumer protection in real estate transactions: raising disclosure requirements of builders, bridging existing information asymmetry between buyers and builders, and ring-fencing the money paid upfront by buyers. About 22 odd states and six union territories have notified the law. But some states have diluted the rules and some have been lethargic in its implementation. Regulation will be on a weak foundation when there is non-transparency in the market for urban land and housing. There is also a fundamental problem in financing these projects that needs to be fixed. Real estate projects are long term, but short term finance is raised to fund them and when the roll-over of funds gets interrupted, projects get stymied. Fixing the problem calls for strengthening the bond markets.



FOOTNOTES

1. <http://www.knightfrank.co.in/blog/2017/09/11/india-among-top-10-price-appreciating-housing-markets-knight-frank-global-house-price-index-q2-2017>
2. India Brand Equity Foundation (IBEF) report on Real Estate (March 2019).
3. India Brand Equity Foundation (IBEF) report on Real Estate (March 2019).
4. Union Budget Speech 2019-20.
5. <https://www.investindia.gov.in/sector/construction>
6. <https://www.ibef.org/download/real-estate-mar-2019.pdf>
7. 'New real estate trends expected to emerge in 2019'(3 January 2019) Livemint <https://www.livemint.com/Money/TARlbPohy7pnqyZxkNLRWL/New-real-estate-trends-expected-to-emerge-in-2019.html>

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